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Chile's Economic Recovery Program

The ruling junta in Chile is moving aggressively to rebuild the economy by adopting a harsh austerity program and instituting policies designed to return the country to a market economy.

Initial Efforts

Faced with shortages aggravated by heavily subsidized prices, Santiago moved quickly after the coup on 11 September to remove price controls on all but 30 basic commodities. The Central Bank also devalued the escudo by some 60 percent and simplified the exchange rate system in an effort to curb import demand and ease pressures on Santiago's meager foreign exchange reserves. As a consequence of the devaluations and relaxed price controls, Chile's cost of living jumped sharply in October, bringing the inflation rate to about 450 percent for the first ten months of the year. Price rises during the last two months of 1973 probably will push inflation to over 750 percent for the year.

The elimination of price controls and adjustment of exchange rates caused the black market rate for escudos to plummet from 2,200 to the dollar to 950. While exchange rates changed and prices rose, the growth in the money supply was sharply curtailed, causing a relative scarcity of local currency and a liquidity crunch for businessmen. To finance business

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activities, holders of dollars are changing them into escudos at official rates in record volumes. Over \$14 million have been converted since mid-November, mostly to finance business operations.

Domestic Impact

Despite a healthy increase in the minimum wage, working-class consumers are finding it increasingly difficult to afford even the barest necessities. Middle income groups are also being hit hard. These conditions have been worsened in many cases by dismissals of relatively unproductive and politically suspect employees hired under the Allende regime. An unemployment compensation program has been announced, but it has not been implemented because of a shortage of trained administrators and a lack of effective coordination. An extensive public works program is under consideration.

The junta has attempted to enlist public support for the austerity program through a series of public jawboning sessions and repeated press conferences, all of them having the theme of highlighting the dismal Allende heritage and the consequent need for belt-tightening. Although business is showing some renewed confidence, consumers and labor appear to be less than enthusiastic about the junta's programs. No organized resistance to the junta or its programs has appeared, however.

Although some leftist groups might seize upon the wage-price squeeze to foment strikes and other violence, the left's ability to mobilize the workers against the regime is questionable, because organizers and militants no longer have easy access to the factories, and the days of regular pay for demonstrating rather than working are over. There is a risk, however, of widespread unrest and spontaneous strikes if pressures on consumers and labor are not eased during the next six months.

External Economic Relations

Chile still faces large balance-of-payments deficits in both 1973 and 1974 even if debt repayments are rescheduled in both years. With the massive \$4 billion foreign debt hanging over Santiago's head, it will at best be several years before Chile's balance-of-payments position improves significantly.

Copper production has already increased more than 50 percent above last year's rate through better worker discipline, a 9-percent lengthening of the workweek, and improved mine management. Production will probably reach a record 750,000 tons next year, but shortages of spare parts, serviceable tractors, and trucks constitute a substantial constraint to further expansion of production.

Another major problem is how to increase agricultural production rapidly. Agricultural imports, the largest drain on foreign exchange, are likely to exceed \$500 million in 1974. The recent sharp increases in agricultural prices provided windfalls to farmers and merchants but will not significantly affect output until the 1974/75 harvest, since most crops are already planted and are well into the growing season. Chile is importing grain to ease domestic shortages and has received \$52 million in US credits for grain purchases. Continuing high world prices as well as adverse world reaction to the coup have compounded Santiago's problems in obtaining adequate grain supplies.

Chile also continues to face shortages of such critical items as spare parts, transportation equipment, aluminum, ferrous scrap, and petrochemicals for textile fiber production. The aluminum shortage resulted from a cutoff in supplies from Hungary and the USSR. Stocks of ferrous scrap are virtually exhausted, and Chile will require imports of over 40,000 tons next year. The US has granted hardship exemptions for the export of 7,000 tons during the remainder of 1973.

While the problems of adequate short-run supplies of raw materials and spare parts must be solved to boost production quickly, long-run growth will depend heavily on Chile's

ability to attract adequate foreign investment. Attraction of substantial new investment, in turn, will depend on the junta's ability to demonstrate good faith in the treatment of foreign equity as well as its ability to instill confidence in Chile's prospects for stable recovery and growth. A critical first step in this area is timely settlement of outstanding compensation claims emanating from the Allende nationalizations. The junta has stated that it will either return intervened firms to the private sector or, as in the case of the large copper mines, compensate the previous owners adequately. Some 88 firms, including five with US interests, are already in the process of reverting to their original owners.

The junta has succeeded in lining up sufficient foreign credits to enable it to purchase capital goods essential to the recovery of production. Private US and Canadian sources have granted nearly \$200 million in new short-term credits, \$215 million has been granted by Argentina, and about \$200 million by Brazil. Colombia is providing an additional \$15-\$20 million in private bank credits.

Prospects

The economic outlook for Chile is cautiously optimistic as the junta takes steps to correct the excesses of nearly three years of state socialism under the Allende regime. The

programs are economically sound and offer a firm foundation for recovery and growth of the economy. The emerging dominance of Raul Saez is probably a positive factor, since the junta's austerity program must be tempered if political as well as economic recovery and stability are to be achieved. Meanwhile, Chile is preparing to settle outstanding compensation issues with the US. Timely resolution of these issues (including an early settlement with Cerro Corporation) would go far in improving international investor and creditor confidence in Chile.